

**LEGISLATIVE SERVICES AGENCY
OFFICE OF FISCAL AND MANAGEMENT ANALYSIS**

200 W. Washington, Suite 301
Indianapolis, IN 46204
(317) 233-0696
<http://www.in.gov/legislative>

FISCAL IMPACT STATEMENT

LS 6423

BILL NUMBER: HB 1336

NOTE PREPARED: Mar 15, 2010

BILL AMENDED: Mar 13, 2010

SUBJECT: Mortgages and Public Deposits.

FIRST AUTHOR: Rep. Bardon

FIRST SPONSOR: Sen. Hershman

BILL STATUS: Enrolled

FUNDS AFFECTED: ☒ **GENERAL**
☒ **DEDICATED**
☐ **FEDERAL**

IMPACT: State & Local

Summary of Legislation: *Five Star Mortgage Program:* The bill establishes a voluntary Five Star Mortgage Program for creditors (including mortgage brokers) that offer qualifying mortgages to Indiana customers after June 30, 2010. It requires the Department of Financial Institutions (Department) to adopt guidelines to implement the program. It provides that to qualify as a five star mortgage lender, a creditor must provide to the Department a certification attesting that the creditor meets specified criteria.

The bill provides that to qualify as a five star mortgage, a mortgage: (1) must require: (A) a down payment of at least 10% of the purchase price of the dwelling, in the case of a purchase money transaction; or (B) that the customer have equity of at least 10% in the dwelling, in the case of a refinancing; (2) must have a fixed rate of interest; (3) must provide for an escrow account for the payment of taxes and insurance, if the creditor regularly provides for such escrow accounts in the creditor's ordinary course of business; (4) may not have a term that exceeds 30 years; and (5) may not include a prepayment penalty or fee. The bill also requires a five star mortgage lender to provide a written statement to any Indiana customer who: (1) applies for a five star mortgage offered by the lender; and (2) does not qualify for the mortgage based on the lender's underwriting standards. It also provides that the statement must set forth the reasons why the customer did not qualify for the five star mortgage.

The bill allows a creditor that qualifies as a five star mortgage lender to include that fact in marketing materials or solicitations directed at Indiana customers, subject to the Department's guidelines. It requires the Department to publish on the Department's Internet web site a list of all creditors that have a current and accurate certification or renewal certification on file with the Department. It requires the Department to provide written notice to a creditor that the creditor does not qualify for the program whenever a creditor: (1) holds itself out as a five star mortgage lender when it does not qualify to participate in the program; or (2) fails to comply with any program requirement. It requires the Department to remove such a creditor from

the list of five star mortgage lenders on the Department's Internet web site and to provide, on the same Internet web page on which the list is published, a link to the notice provided to the creditor.

The bill provides that the authority of the boards of trustees of the Public Employees' Retirement Fund (PERF) and of the State Teachers' Retirement Fund (TRF) to invest in pooled funds includes the authority to invest in pools consisting in part or entirely of five star mortgages. It allows the PERF board to maintain alternative investment programs within: (1) the PERF annuity savings account; and (2) the legislators' defined contribution plan; that invest in pooled funds consisting in part or entirely of five star mortgages, or that otherwise invest in five star mortgages. It also allows the TRF board to maintain alternative investment programs within the TRF annuity savings account that invest in pooled funds consisting in part or entirely of five star mortgages, or that otherwise invest in five star mortgages.

Local Board of Finance Meetings: The bill removes the discretion of a school corporation to determine whether a local board of finance meeting is needed on an annual basis.

Investment of Public Funds: The bill permits local government investment officers to invest in municipal securities issued by an Indiana local governmental entity, a quasi-governmental entity related to the state, or a unit of government, municipal corporation, or special taxing district in Indiana so long as the issuer has not defaulted on an obligation within the 20 years preceding the date of the purchase.

The bill permits counties and political subdivisions to invest public funds in certificates of deposit under certain conditions. The bill removes the prohibition against investing not more than 50% of a unit's depository funds in money market mutual funds.

Depository Placement: The bill replaces the requirement that money be invested in transaction accounts and certificates of deposit with the depository quoting the highest interest rate with the authority to invest in a depository offering any one of the top three interest rates so long as the reason for choosing the alternate depository is noted in the memorandum of quotes.

Board for Depositories - Members, Meetings, and Other Procedures: The bill changes the appointments to Board for Depositories to require one appointment by the Speaker of the House of Representatives, one appointment by the President Pro Tempore of the Senate, and two appointments (instead of four) by the Governor. It requires one of the appointees by the Governor to be a chief executive officer or a chief financial officer of a depository that is a state chartered credit union in Indiana. The bill requires that each of the four appointed members be a chief executive officer or a chief financial officer of a depository and that each appointment represent a different segment of the financial institutions industry. It provides that if the depository is not domiciled in Indiana, the appointee must be the most senior corporate officer of the depository with management or operational responsibility or the person designated to manage public funds for the depository that is located in Indiana. It specifies that the term of an appointed member is four years. It permits the appointing authority to reappoint a member if the individual meets the requirements at the time of reappointment. It provides that a simple majority of the Board members voting is required to approve an action by the Board, instead of a unanimous vote. It requires the Board to hold a public meeting at least once each calendar quarter. It requires that deliberations concerning a particular financial institution be held in executive session by the Board and provides that records related to these matters are confidential. It requires the Board to prepare a general summary semiannual report and present it to the Budget Committee. It changes the requirement for meeting notices from ten days to two days. It also eliminates a report by the Public Employees' Retirement Fund to the Board's secretary-investment manager and an interest calculation concerning the coverage of local police and firefighter pension funds.

Board for Depositories - PDIF: The bill allows the Board to fix the assessment rate at the times the Board determines to be necessary instead of twice each year. It exempts certain certificates of deposit issued by a federally insured bank or savings and loan association from the assessment calculation. It provides that the Board may consider capital adequacy, liquidity, and asset quality in addition to any study by actuaries in establishing any change in the reserve for losses. It exempts federally insured deposits from the assessment calculation. It also provides an exemption from assessment for a public depository if it pledges acceptable collateral equal to the public deposits it holds and the collateral level was continuously maintained for the 12 months immediately preceding an assessment.

The bill increases from \$1,500,000 to \$300,000,000 the amount of anticipatory warrants the board may issue to pay immediate claims when the assets in the Public Deposit Insurance Fund (PDIF) are not sufficient to pay claim.

Board for Depositories - Collateral on Certain Public Funds Deposits: The bill permits the Board to accept as collateral bonds or other obligations that the Board could not invest in if the Board determines the obligations are acceptable collateral. It specifies that United States Treasury securities, Federal agency securities, and irrevocable letters of credit issued by a Federal Home Loan Bank are acceptable collateral. It permits the Board to determine whether a depository may withdraw collateral when the amount of public funds on deposit is at least 10% less than the market value of securities pledged as collateral. It allows the Board to determine the amount and type of substituted securities a depository may provide to insure the insurance fund's solvency consistent with the depository's pro rata share of total deposit accounts of public funds based on an average of the depository's total public deposits. It provides that if the PDIF balance reaches zero, all depositories must pledge collateral equal to 100% of the depository's public fund holdings. It also provides that the market value of the substituted securities as of the date of delivery may be less than, but may not exceed, the amount determined by the Board.

Public Depositories that are Credit Card Issuers: The bill provides that a financial institution may not have public funds on deposit if it issues a credit card as a card issuer and the institution is not in substantial compliance with the federal Credit Card Accountability Responsibility and Disclosure Act of 2009 and requires the Department of Financial Institutions to investigate complaints and determine whether a financial institution is in substantial compliance with the act..

Joint Investment Funds: The bill provides that a joint investment fund may be invested or reinvested only in investments that are permitted for political subdivisions.

Pension Distribution Fund Distributions: Changes the distribution from the Pension Distribution Fund to local units into a distribution to the Pension Relief Fund from which distributions are made to local units.

Effective Date: Upon Passage; July 1, 2010; January 1, 2011.

Explanation of State Expenditures: *Five Star Mortgage Program:* This bill will require DFI to (1) adopt guidelines to implement a five star mortgage program, (2) publish a list of creditors who have accurately self-certified to be five star lenders, and (3) investigate credible complaints of lenders falsely purporting to be five star lenders. DFI reports the provisions of this bill can be implemented with existing staff and resources.

Public Employee Retirement Fund (PERF) and Teacher's Retirement Fund (TRF): This bill allows the PERF and TRF executive boards to invest retirement funds in pooled funds that consist either entirely or in part

of five star mortgages. Providing these mortgages as investment options will increase the number of options available to investment managers. Assuming five star mortgages are a good investment, these options may be selected over less appealing ones. These provisions are not necessarily expected to impact state expenditures or workload, but rather expand the options available to managers investing the public funds of PERF and TRF.

Board for Depositories: The bill makes changes to the appointing authorities and qualifications for the appointed members of Board for Depositories. The bill also changes procedures of the Board including the necessary number for approval of items and the reduction of amount of notice necessary before a meeting of the Board. None of these changes is expected to have fiscal impact.

Under current statute, the Board consists of the Governor, the State Treasurer, the State Auditor, the Chairman of the Financial Institutions Commission, the Chief Examiner of the State Board of Accounts, and four members appointed by the Governor who are Indiana residents and have had substantial expertise in commercial lending with depositories. Under the bill, the Governor would appoint two Board members, the Speaker of the House of Representatives would appoint one Board member, and the President Pro Tempore of the Senate would appoint one Board Member. Each of the appointed members must be a CEO or CFO of a depository at the time of appointment, if it is an Indiana Bank. If the depository is not an Indiana Bank, the appointee must be the most senior corporate officer of the depository with management or operational responsibility, or a person designated to manage public funds, for the bank's depository in Indiana. The bill requires the Governor to provide for geographic representation of all regions in making the two Governor's appointments. The bill also requires the appointed members to come from different types of depositories. One of the Governor's appointees must be from a state chartered credit union. The remaining three appointees must be from a depository that is not a state chartered credit union with: (1) deposits of less than \$250 M for the Governor's other appointee; (2) deposits between \$250 M and \$1,000 M for the President Pro Tempore's appointee; and (3) deposits exceeding \$1,000 M for the member appointed by the Speaker of the House. These qualifications changes would affect appointments made after June 30, 2010.

Explanation of State Revenues: *Five Star Mortgage Program:* This bill will increase state revenue from certification fees for five-star lenders, from any civil penalties assessed against individuals who violate provisions of the five-star program, and any additional revenue collected from civil court fees. Increases in state revenue is indeterminable.

This bill will allow DFI to collect certification fees for the five-star lending program. Increases in revenue will depend on the number of creditors who apply to be a five-star lender and the application fee established by DFI.

Deposit and Investment of Public Funds: The bill will have indeterminate fiscal impact on state and local government concerning the rate of return and the amount of risk on money in funds controlled by the investing officer and available for investment. Details of the changes follow:

Investment of Public Funds - The bill would do the following:

- (1) The bill would allow a state or local officer to invest public funds in: (a) municipal securities issued by an Indiana local governmental entity, quasi-governmental entity, municipal corporation, or special taxing district, provided the issuer hasn't defaulted on obligations in 20 years; or (b) certificates of deposit in federally insured banks or savings and loans.
- (2) The bill would allow a state or local officer to invest more than 50% of the unit's depository funds in

money market mutual funds. Current statute restricts these investments to no more than 50% of a unit's depository funds.

(3) The bill would prohibit a state or local officer from depositing public funds in a financial institution that issues an unsecured credit card, as a card issuer, and the financial institution is not in substantial compliance with the federal Credit Card Accountability Responsibility and Disclosure Act of 2009.

These provisions of the bill could change the make up of portfolio held by state or local government with indeterminate fiscal impact on the return and risk.

Depository Placement - Current law requires an investment officer to accept the bid of a depository that offers the highest rate of return for investment of funds in certificates of deposit. The bill allows the investment officer to place funds in a certificate of deposit with a depository quoting the second or third highest rate of interest and noting the reason for the placement. The rate of return would be diminished, but potentially local depositories could receive more deposits even if they are not paying the highest rate of interest available.

Board for Depositories: Other changes to the Board's procedure concerning the Public Deposit Insurance Fund (PDIF) have indeterminate fiscal impact. The bill allows the Board to set the assessment rate to provide assets in the PDIF more than twice a year up to the current law maximum of 2%. The bill also increases the limit on anticipatory warrants issued by the Board to pay claims on the PDIF from \$1.5 M to \$300 M.

The PDIF is maintained and operated by the Board and insures the deposits of all public money in Indiana depositories. The PDIF is funded by assessments payable by every depository that holds public funds. The PDIF assessment was suspended in 1985, but until that time it was a monthly fee not to exceed 2% of the sum of the minimum public fund balances that public funds depositories held during the month. As of June 30, 2009, the net assets of the PDIF totaled \$308,222,700.

Civil Penalties: Under the bill, creditors who are found to have violated provisions of the five star lending program can be subject to civil penalties. This will increase state revenue (1) to the extent individuals are found in violation of the program's provisions, (2) if retribution is sought through the civil process, and (3) awards made by the court. Actual increases are indeterminable.

Court Fee Revenue: If additional civil actions occur and court fees are collected, revenue to the state General Fund may increase. A civil costs fee of \$100 would be assessed when a civil case is filed, 70% of which would be deposited in the state General Fund if the case is filed in a court of record or 55% if the case is filed in a city or town court. In addition, some or all of the document storage fee (\$2), automated record keeping fee (\$7), judicial salaries fee (\$18), public defense administration fee (\$3), court administration fee (\$5), and the judicial insurance adjustment fee (\$1) are deposited into the state General Fund. Additional fees may be collected at the discretion of the judge and depending upon the particular type of case.

Explanation of Local Expenditures: *Five Star Mortgage Program:* This bill may increase the workload of local courts if more civil cases are heard for violations of the five-star lending program. Actual increases are unknown.

Explanation of Local Revenues: *Local Investment Requirements:* The changes outlined above for investment in the *Explanation of State Revenues* concerning public funds are also made relative to investment of public funds by county treasurers or fiscal officers of political subdivisions.

Court Fee Revenue: If additional civil actions occur, local governments would receive revenue from the following sources. The county general fund would receive 27% of the \$100 civil costs fee that is assessed in a court of record. Cities and towns maintaining a law enforcement agency that prosecutes at least 50% of its ordinance violations in a court of record may receive 3% of court fees. If the case is filed in a city or town court, 20% of the court fee would be deposited in the county general fund and 25% would be deposited in the city or town general fund. Additional fees may be collected at the discretion of the judge and depending upon the particular type of case.

State Agencies Affected: State Treasurer; Board for Depositories; Department of Financial Institutions; Attorney General.

Local Agencies Affected: Local units with investment responsibilities; Local courts.

Information Sources: John Schroeder, DFI.

Fiscal Analyst: Jim Landers, 317-232-9869; Bill Brumbach, 232-9559; Jim Sperlik, 232-9866.